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C O N F I D E N T I A L SECTION 01 OF 03 SOFIA 000641

SIPDIS

FOR SPECIAL ENVOY BOYDEN GRAY

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TAGS: [ECON](#) [ENRG](#) [PGOV](#) [BU](#)

SUBJECT: BULGARIA AND THE ENERGY KNOT: SCENESETTER FOR OCT
7 VISIT OF SPE GRAY

Classified By: Ambassador Nancy McEldowney for reasons 1.4. (b) and (d)

1. (C) Summary: The quandary over energy facing all our European partners is particularly acute here in Bulgaria. With few hydrocarbons of its own, Bulgaria relies on Russia for seventy percent of its total energy needs and over ninety percent of its gas. Though previously a net exporter of electricity, the EU's decision to force closure of blocks 3 and 4 of the communist-era nuclear plant Kozluduy cost the Bulgarian economy over USD 1.4 billion and put a squeeze on Serbia, Macedonia and Greece, who had purchased the bulk of the exports. The hard reality of today's energy picture is that Russia is not only the dominant supplier, it is also the dominant player -- your visit here is the first by a senior U.S. energy official in a year, whereas Putin has personally engaged both the President and Prime Minister on energy issues in multiple sessions over the past ten months. But the cartoon strip portraying a passionately eager Bulgaria in bed with the muscle bound duo of Gazprom and Lukoil is only partially true -- it is a tryst driven less by passion and more by a perceived lack of options. Prime Minister Stanishev recently described Russian tactics on South Stream as blackmail and Energy Minister Dimitrov complains openly of psychological warfare. At the same time, the Bulgarians are deeply worried about the prospects for Nabucco and are convinced that Azeri gas supplies will be held up by Turkey. Their bid to hold an energy summit in the spring, the ostensible focus of your visit, is designed to catalyze greater coordination -- and negotiating leverage -- amongst transit countries while also getting the United States more actively engaged. Background on specific issues likely to arise in your discussions with President Parvanov, Prime Minister Stanishev, Foreign Minister Kalfin and Energy Minister Dimitrov follows below. End Summary.

TIMING

2. (C) Your visit to Sofia comes when Bulgaria is striving to sell itself as a European energy center. With six active or potential pipelines transiting the country, the creation of a new energy mega-holding company, and the construction of a new nuclear plant, Bulgaria is setting itself up to be an important regional energy player, despite being overly dependent on Russian energy sources. The proposal to host a major gas summit in April 2009 -- which Putin has already promised to attend -- is the latest attempt to put Bulgaria on the energy map. Your visit will guide the Bulgarians as they formulate an agenda and goals for this summit. It will also focus Bulgarian policy makers on U.S. views on Russian energy strategy and South Stream, answer growing skepticism about Nabucco's prospects, and give solid counter-arguments to those who say there is no real alternative to dependence

on Russian energy.

THE SUMMIT

13. (C) At the January 19 signing of the South Stream Intergovernmental Agreement, President Parvanov, with Putin at his side, announced Bulgaria would host an energy summit intended as a follow-on to the June 2007 Zagreb energy conference. Upon Putin's departure, Sofia fell under heavy criticism both at home and abroad for hastily joining South Stream, and the energy summit idea lost steam. Ambassador for Energy Security Peter Poptchev told us the Bulgarians resented perceived Russian pressure to hold such a summit. In July the Bulgarians independently resurrected the summit idea as a way to show Bulgarian support for Nabucco and diversification, as well to balance European, U.S. and Russian interests in the Caspian and Black Sea regions. With the potential for six pipelines passing through its territory, the Bulgarians also have high hopes to become a regional energy hub. The summit, they believe, will help put Sofia on the map not only as an energy center, but as a place that brokers discussions between the West, Russia and Eurasia.

14. (C) The Bulgarians requested your visit to advise on the summit. They envision a spring conference (tentatively April 24-25) that would bring together heads of state from Eurasian and European producer, transit and consumer countries. PM Stanishev told Ambassador September 19 that Putin has agreed to attend. The summit will be gas-focused and will attempt to put "real solutions" on sources, routes and quantities on the table. Well-aware of the potential for East European energy conference fatigue in the first half of 2009, the Bulgarians are proposing that all key participants, including the EU, the United States and Russia, view the proposed Hungarian, Bulgarian and Czech conferences as a linked continuum. The April Sofia conference would take care of any unfinished business left from the January Hungary Conference and the proposed Czech conference would take up where the Sofia conference leaves off. To distinguish the Bulgarian summit, Sofia is considering including an as-yet undeveloped "industry component."

15. (C) The Bulgarians will seek U.S. views and your advice on the proposed agenda of the summit and whether it will advance U.S. goals in the region. They want recommendations on how to coordinate the Hungarian, Bulgarian and Czech conferences and may seek advice on the proposed industry component of the Sofia summit. They are interested in, but may not ask directly about, U.S. views on whether Sofia has a future as an intermediary between Europe, the United States and Russia on energy and other issues affecting the Black Sea region. They are interested in your analysis of recent Azeri and Turkish energy moves. They will also request high level U.S. attendance at the summit.

BULGARIAN ENERGY PROJECTS

16. (C) SOUTH STREAM: The Bulgarians signed the South Stream intergovernmental agreement in January and Parliament ratified the agreement in July. Negotiations between Bulgargaz and Gazprom resumed in September to work out a pre-shareholders agreement. At our recommendation, and at the direction of the Government, state-owned Bulgargaz reluctantly hired outside legal counsel (the U.S. law firm Paul Hastings) to represent it in South Stream negotiations. With the creation of a new, state-owned energy mega-holding in September, Bulgargaz has lost much of its previously-considerable independence. The acting head of the Bulgarian Energy Holding is Deputy Energy Minister Galina Tosheva, previously lead South Stream negotiator for the Bulgarian Government. Tosheva has a healthy suspicion of Russia's intentions in Bulgaria and has directed Bulgargaz to rely on its legal counsel for expert advice. Tosheva told us that Gazprom negotiators are taking a hard line now that negotiations have resumed. They are proposing to re-route

gas currently transiting Bulgaria (for which Bulgartransgas makes a healthy profit) to South Stream, meaning South Stream would not represent 31 bcm of new gas for Europe, but something significantly lower. The Bulgarians state that this is contrary to the spirit of the IGA and are preparing to fight the Russian proposal.

¶17. (C) NABUCCO: Despite the strong public support they have shown Nabucco this year, the Bulgarians are turning into Nabucco-skeptics. In March, Sofia signed what it thought was an agreement for Azerbaijan to supply 1 bcm of gas that Bulgaria would eventually take as its Nabucco quota. In advance of Nabucco, Bulgaria planned to access the gas via a potential hook-up to the Turkey-Greece-Italy interconnector. Realizing now that the agreement was not, in fact, a commitment on Azerbaijan's part, the Bulgarians feel burned. The government is now in dire need of a pep talk on the Nabucco. They state firmly that both South Stream and Nabucco are critical and that one cannot be allowed to preclude the other. At the same time, they are nervous about both Azerbaijani willingness to supply Nabucco and Turkish willingness to support the project. They will be interested in your view of Nabucco's prospects.

¶18. (C) TGI HOOK-UP: The Bulgarians are in negotiations with Greece about this possible interconnector. Energy Holding CEO Tosheva said this is Bulgaria's most immediate source of diversification and energy security. The Greeks apparently are cool to the idea, saying there is insufficient gas. In response, the Bulgarians have proposed the purchase of LNG to be delivered to Greece in exchange for either TGI access or gas currently going through the export pipeline from Russia and transiting Bulgarian territory. Your Bulgarian interlocutors may ask for U.S. support for these schemes in our discussions with the Greeks and Turks.

¶19. (C) BURGAS-ALEXANDROUPOLIS (BAP) and AMBO: The Bulgarians, Russians and Greeks signed a shareholders agreement for the BAP oil pipeline in January during the Putin visit. Since then, the project company has been registered, but little more progress has been made. The Bulgarians are still confident the pipeline will be built, and seem surprisingly uninterested in the dynamics surrounding CPC expansion. With BAP's relative progress, the AMBO (Albania-Macedonia-Bulgaria) oil pipeline project has lost momentum. Still, Bulgaria remains committed to AMBO and is ready to move forward if and when AMBO attracts supply and financing.

¶10. (C) BELENE: In 2006 the GOB selected Russian AtomstroyExport as the contractor for the new Belene nuclear plant. Bulgaria is keeping majority ownership of the plant, but is in the process of selecting a strategic investor for the other 49 percent. RWE and the Belgian Electrabel are in the running. We have stated repeatedly that the choice of a Russian contractor for Belene decreased Bulgaria's bid for greater independence from Russian energy sources. The lack of transparency surrounding the tender has led to the inescapable conclusion that the decision to choose Russia as the Belene contractor was linked to the re-negotiation of Bulgaria's long-term gas transit contract with Gazprom in December 2006.

YOUR MEETINGS

¶11. (C) President Parvanov began his second five-year term in 2007. Parvanov's desire to exercise behind-the-scenes influence over the government has led to tensions with his former protege, Prime Minister Sergei Stanishev. Parvanov has close ties to Russian politicians and held no less than eight meetings with Vladimir Putin in the last seven years. The energy summit will be under his aegis.

--Prime Minister Sergei Stanishev is a 42-year-old progressive Socialist. He is pro-west and eager to have Bulgaria viewed as a good friend and partner of the United States. He returned September 30 from a week-long visit to

the United States where he met with U/S Burns, spoke at the Harvard Business School and held an investment forum. He understands that Bulgaria is overly dependent on Russian energy sources, but sees Bulgaria as having few options for greater energy independence.

--Foreign Minister Kalfin is close to both Stanishev and Parvanov and as Deputy Prime Minister oversees the Economy and Energy Ministry. He is a strong supporter of close Bulgarian-U.S. relations and is highly conversant on energy issues.

--Economy and Energy Minister Petar Dimitrov is a relative new-comer to energy issues. He is largely seen as taking direction on energy matters from former Energy Minister Rumen Ovcharov, who is linked with Russian energy interests and left office in June 2007 after a corruption scandal.

112. (C) Your visit will also highlight, though meetings and press outreach, the need for Bulgaria to focus on a long-term energy strategy not solely based on the transit of hydrocarbons or the production of Russian-based nuclear energy, but on the development of renewables, clean coal and greater energy efficiency. Bulgaria will always be dependent on Russian energy to one extent or another. But as the most energy inefficient economy in Europe, it can make meaningful strides toward greater diversity away from Russian energy sources. With the price of energy at near record highs, Russia's hydrocarbon-generated wealth is increasingly circulating through the Bulgarian economy, making Bulgaria all the more susceptible to Russian leverage. An energy strategy that focuses on renewables and efficiency is one tool Bulgaria can use to put a noticeable dent in negative Russian influence. The other tool is transparency. Hub status in any industry is bestowed only on places which offer transparent, efficient service. To achieve its goal of becoming a true energy center, we should recommend that Bulgaria present itself not as the place with closest ties to Russia, but as the most transparent place to do energy deals.

McEldowney